

CALIFORNIA PUBLIC UTILITIES COMMISSION
Water Division

STANDARD PRACTICE FOR PROCESSING
CONSUMER PRICE INDEX, RATE BASE
AND EXPENSE
OFFSET RATE INCREASES AND
AMORTIZING RESERVE,
MEMORANDUM AND BALANCING ACCOUNTS

Standard Practice U-27-W

SAN FRANCISCO, CALIFORNIA
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STANDARD PRACTICE FOR PROCESSING CONSUMER PRICE INDEX, RATE
BASE, AND EXPENSE OFFSET RATE INCREASES AND AMORTIZING RESERVE
AND MEMORANDUM ACCOUNTS

A - PURPOSE AND DEFINITIONS

1. The **purpose** of these procedures is to ensure a uniform and complete method of processing offset rate increase and reserve and memorandum account amortization advice letters. All regulated water utilities and the Water Division (WD) engineer or analyst (analyst) shall use these procedures, unless a deviation is approved by the Director of the Water Division.
2. The use of a **CPI offset** was approved on March 31, 1992, when the Commission issued Decision 92-03-093 authorizing Class C and D water utilities to file once each year by advice letter for a rate increase based on the most recent year-end increase in the Consumer Price Index for All Urban Consumers (CPI-U) announced by the Bureau of Labor Statistics, U.S. Department of Labor. Any water utility presently earning less than the rate of return authorized in its most recent rate case and not subject to a second test year or attrition year adjustment was authorized to file once each year by advice letter for this CPI-U increase. Any utility that misses filing during a year may not file retroactively during the next year. Decision 99-10-064, October 21, 1999 in the Mergers and Acquisition Rulemaking, R.97-10-048, extends this offset to a Class B or A utility that purchases an Inadequately Operated and Maintained Water System (a system with less than 2,000 service connections that had an outstanding order or citation from the California Department of Health Services when it was acquired) for that system's customers up to seven years after the purchase date.
3. Class A utilities may be authorized authority to file a **rate base offset** only by decision. Class B, C and D utilities may file for a rate base offset without prior authorization. Rate base offsets do not have an associated reserve account. As with CPI offsets, any rate base offset that was not authorized in a general rate case requires an earnings test. Rate base offsets are available for used-and-useful utility plant only and the offset may be subject to a saturation adjustment¹ if the facilities are over-built.
4. **Expense offsets** were authorized by statute in 1976. Expense offsets were originally for electric utilities to track and recover fuel costs. The Commission established rules for

¹ See U-3-SM "A saturation adjustment is a procedure whereby excess or overbuilt utility plant, financed or installed with equity capital, is excluded from rate base in determining the rates a utility is authorized to charge for service. Water Division procedures and Commission policy are based on precedent set in Decisions No. 50971 (1/10/55) and No. 56261 (2/18/58) in Application No. 34541 by Big Bear Pines Water Company. The Commission reasoned that an adjustment was proper to protect the interests of rate payers in those situations where an extensive water system has been constructed but with a significant portion of the lots to be served remaining undeveloped for an extended period following initial construction of the water system. This adjustment, in time, became known as a saturation adjustment and has been used by the Water Division and adopted in numerous proceedings. Uses of this adjustment occurred in Decision No. 92796 (3/17/81) in Application No. 59530 by Freshwater Valley Estates Water Company and in Resolution No. W-3004 (7/21/82) for Bear Trap Ridge Water Company."

applying them to water utilities on June 28, 1977², and rules for calculating them on September 6, 1978³. The 1977 policy included a means test (Conclusions and Recommendations, p. 1, recommendation (c)):

“Traditional test for offset proceeding be continued. These require, that with the offset, the rate of return not exceed that last authorized by the Commission and the amount of the offset not exceed the revenue increase(sic.).”

but the 1978 policy did not. The 1978 policy did do the following:

- a. “The maintenance of balancing accounts for any given item will start from the date the Commission first authorizes new rates passing through specific changes in cost... all subsequent changes in cost of that item would be recorded in the balancing account as they occur.”
- b. “Utilities should maintain three types of balancing accounts. A balancing account for all types of water production cost offsets including purchased water and purchased power, a balancing account for ad valorem tax offsets and a balancing account for all other types of offsets.”

The 1978 policy went out to all Class A and B utilities.

At one time there was a lower limit of 1% and an upper limit of 10% on offsets, but that was modified in 1979 to simply require individual customer notice for increases over 10%⁴. The 1% lower limit, based on the most recent test year or the most recent annual report revenues, remains⁵.

The Commission authorized additional changes in the calculation procedure on May 18, 1983⁶. These guidelines clearly show an expense increase followed in a few months by an of-setting revenue increase. They also provide formulas for phasing in the expense revenue increase.

These guidelines were consolidated in 1984⁷. No offsets are allowed if the latest adopted quantities are more than 5 years old (p. 6).

² Memorandum to the Commission from B. A. Davis, Director Operations Division, June 21, 1977, approved 6/28/1977 Commission Conference, Subject: Major Water Utilities Regulatory Policy

³ Memorandum to the Commission from B. A. Davis, P. L. Boneysteele, W. H. Cavagnaro and Janice E. Kerr, adopted September 6, 1978, Subject: Procedure for Maintenance of Balancing Accounts for Water Utilities

⁴ Memorandum to All Hydraulic Branch Engineers from John D. Reader, December 13, 1979, Subject: Policy Matters

⁵ Memorandum to All Hydraulic Branch Technical Staff from Wesley Franklin, Chief, Hydraulic Branch, November 9, 1984, Subject: Procedures for Offset Rate Increases, attachment, p. 2

⁶ Memorandum to the Commission from William Ahern, Barbara Barkovich, Bruno Davis and Jan Kerr, April 18, 1983, Subject: Procedure for Maintenance of Balancing Accounts for Water Utilities (Commission Conference of May 18, 1983)

⁷ Memorandum to All Hydraulic Branch Technical Staff from Wesley Franklin, Chief, Hydraulic Branch, November 9, 1984, Subject: Procedures for Offset Rate Increases

Expense offsets allow a utility to pass on to the customer changes in certain costs that are considered to be beyond the utility's control and that are in the public interest to allow the utility to recover. Since expense offsets allow dollar-for-dollar recovery of these expenses, they are tracked using a reserve account (see below) and may be booked for accrual recovery when they occur. Off-settable expenses include, for all water and sewer service utilities:

- a. purchased power (electricity or natural gas that the utility buys from the energy company),
- b. purchased water,
- c. groundwater extraction charges (pump taxes), and
- d. costs booked to a memorandum account found reasonable for recovery.

Class C and D utilities⁸ are not covered by attrition and may request an offset for:

- e. employee labor,
- f. payroll taxes,
- g. that portion of contract work that is for operation and maintenance of plant facilities (Class D only),
- h. unanticipated repair costs⁹

5. In the summer of 2001, several water utilities filed advice letters seeking offset rate increases to compensate for recent increases in the costs of purchased power. The Office of Ratepayer Advocates (ORA) protested the request to raise the rates of 20 districts of California Water Service Company (CWS), arguing that: (1) the Commission should not authorize offset rate increases for CWS districts because the utility was "over earning," that is, it was earning a rate of return greater than that authorized in the utility's last general rate case; and (2) the Commission should not permit water districts that are outside their rate case cycle to utilize balancing account treatment.¹⁰

6. In response, the Commission's Water Division drafted Resolution W-4294, dated November 29, 2001, which researched the history, rationale, and procedures for implementing offset rate relief and related balancing accounts. The Water Division staff concluded that: (1) ORA's protest raises serious issues of first impression warranting full Commission consideration; and (2) the Commission should consider ORA's recommendations on an industry-wide basis. The Commission agreed with staff's recommendations and issued Order Instituting Rulemaking (OIR) 01-12-009 which in D.03-06-072 imposed an earnings test on offset expense recovery.

7. A **reserve account** must be used for each offset except CPI and rate base offsets. This account tracks the lost revenue (or additional revenue if the offset is a cost decrease) from the time of the change in the offsettable expense until the change is included in base rates. Also, after base rates have been changed to offset an expense change, the utility tracks the actual extra revenue earned by the incremental rate change against the actual incremental expenses incurred by keeping a reserve account (see Public Utilities Code section 792.5). These reserve

⁸ Memorandum to All Hydraulic Branch Technical Staff from Wesley Franklin, Chief, Hydraulic Branch, November 9, 1984, Subj: Procedures for Offset Rate Increases, attachment, p. 1

⁹ D.92-03-093, March 31, 1992, Ordering Paragraph 2.

¹⁰ According to ORA, districts that failed to apply for a general rate case when they had an opportunity to do so, either according to the Rate Case Plan adopted in Decision (D.) 90-08-045, 37 CPUC2d 175, or by other Commission decision, would be outside of their rate case cycle.

accounts are “zeroed-out” as part of a General Rate Case or may be amortized by advice letter. Reserve account balances are recovered by means of a temporary surcharge or surcredit.

8. A **memorandum (memo) account** accrues expenses and the carrying cost and depreciation on capital investments, and offsetting revenues such as insurance proceeds, when authorized by the Commission. Memo accounts track costs and revenues as reserve accounts do, but recovery of these costs is not guaranteed, as it is for reserve accounts (after reasonableness review and a means test). Example memo account expenses include legal fees, watershed study costs, Department of Health Services (DHS) costs (except penalties) and other events of an exceptional nature that are not under the utility’s control, could not have been reasonably foreseen in the utility’s last general rate case, that will occur before the utility’s next scheduled rate case¹¹, are of a substantial nature in that the amount of money involved is worth the effort of processing a memorandum account and that have ratepayer benefits¹². A memorandum account is not recorded in the utility’s accounting books; it represents off-book accounting records. New memorandum accounts may be requested by advice letter requesting approval of a change to the preliminary statement to include a description of the memorandum account. Advice letter memorandum account recoveries require an earnings test and proof of reasonableness.

9. A **balancing account** is necessary to track the balance that the Commission has authorized for recovery or amortization. It is a deferred debit account in the utility’s accounting books. It records an expense authorized by the Commission for recovery or overcollection authorized for refund and the sum of received or allowed surcharges or surcredits. Each district has one balancing account for each separate item to be recovered or amortized. When a balance in a reserve account or memo account is authorized for recovery, that reserve or memo account is moved to a balancing account. If the amount authorized for recovery is less than the amount booked to the reserve or memo account, the unrecovered amount is amortized below the line. As surcredits or surcharges are provided or received, they are booked to the balancing account also. When the balancing account balance reaches zero or a small amount, the surcharge or surcredit terminates and the amount is rolled into another balancing account. Balances in the balancing account earn at the 90-day commercial paper rate.

B - GENERAL PROCEDURE

10. **CPI Offsets.** Early each calendar year the Water Branch will prepare a letter to all Class C and D water and sewer system utilities explaining how to apply for a CPI offset, including the CPI percentage increase to use. A utility calculates a CPI offset by multiplying all service and commodity rates in its existing rate schedules by one plus the percent contained in the letter from the Water Branch.

11. **Expense Offsets.** When a utility incurs a change in an offsettable expense resulting in an annual revenue requirement change of over 1%, it should submit an advice letter requesting an offset in base rates to account for that change. A utility’s advice letter

¹¹ For these first three requirements see Decision 94-06-033, June 22, 1994, page 51

¹² For example, a memorandum account to book legal costs to fight a takeover by a potentially incompetent entity might have ratepayer benefits, but a memorandum account to book legal costs to fight a takeover by a competent water district would not.

requesting an offset rate change should include a citation to the decision or other Commission document approving tracking of each type of expense requested, except for purchased power, purchased water and pump tax expenses.

12. **Reserve Accounts.** Pursuant to Section 792.5 of the Public Utilities Code, the utility must establish a reserve account for each item for which revenue offsets have been authorized. The account must be described in the Preliminary Statement of the utility's tariffs (except for purchased water, purchased power and pump tax). The reserve account tracks the revenues recovered by the rate offset and the offsettable costs incurred (See Appendix A). The average in the reserve account each month accrues interest at the current 90-day commercial paper rate¹³.

13. For Class B, C and D utilities, when the total in the reserve account(s) exceeds (positive or negative) 2% of the gross operating revenue authorized in the last GRC or realized in the last annual report, whichever is higher, the reserve account must be amortized. If the balance is less than 2%, the amount will normally not be amortized outside of a general rate case unless some expenses are approaching two years old. Class A utilities must file by March 31 of each year for recovery or refund of any reserve accounts. Undercollected reserve accounts are amortized by a surcharge on the service charge or the commodity charge, depending upon the type of expense being offset¹⁴. An overcollection in a reserve account is refunded by a surcredit applied only to service charges¹⁵. The reserve account amortization requires a means test based on recorded quantities (See Appendix H).

14. Surcharges and surcredits are described in the Special Conditions section of the applicable tariff sheets. They become effective on the effective date of the tariff sheet. A surcredit will be recovered as soon as possible by reducing the service charge. The maximum length that a surcharge or surcredit will run (in months) must be included in the description. Surcharges or surcredits terminate automatically when the account has been amortized.

15. **Memorandum Accounts.** Memorandum accounts must be requested by advice letter. They become effective on regular statutory notice unless suspended or rejected¹⁶. The advice letter must add a description of the account in the Preliminary Statement (see Appendix B). Each request must address the following:

- a. The expense is caused by an event of an exceptional nature that is not under the utility's control;
- b. The expense cannot have been reasonably foreseen in the utility's last general rate case and will occur before the utility's next scheduled rate case;
- c. The expense is of a substantial nature in the amount of money involved; and
- d. The ratepayers will benefit by the memorandum account treatment.

¹³ One-twelfth of the most recent month's interest rate on Commercial Paper (prime, three months), published in the Federal Reserve Statistical Release, G.13, or its successor publication. See <http://www.federalreserve.gov/releases/H15/data/m/fp3m.txt>

¹⁴ Letter from Wesley Franklin to All Class A, B and C Water Utilities, dated September 13, 1983

¹⁵ The water utilities originally proposed that all amortization of balancing accounts be applied to the service charge. Staff proposed that the proper way of amortizing water supply expenses be through the commodity charge (Letter from Wesley Franklin to Class A, B and C Water Utilities, September 13, 1983).

¹⁶ Southern California Edison Company v. Public Utilities Commission, (2000) 185 Cal. App. 4th 1086.

16. Balances in a memorandum account also earn at the 90-day commercial paper rate¹⁷. Recovery of a memorandum account requires full justification of all expenses and a recorded earnings test for the calendar period during which the expense was incurred. Recovery of memorandum accounts should be spread across all utility services that have benefited from the actions that resulted from the money spent and booked to the memorandum account. For example, recovery of DHS memorandum accounts (not water quality memorandum accounts) should be spread across services such as private fire protection service and reclaimed water because DHS monitors backflow prevention protections for these services. Recovery of water quality memorandum accounts, however, should come only from customers who use potable water. Recovery of memorandum accounts may be done by resolution, which converts the memorandum account into a balancing account and institutes a surcharge or surcredit.

C – FORM AND CONTENTS OF THE ADVICE LETTER REQUESTING RECOVERY

17. Class D utilities may elect to furnish only the following information for offset rate increases:

- a. A written request, including an explanation for the increase costs;
- b. A tabulation of increases in expenses and revenues;
- c. Copies of paid bills and work papers showing calculations in support of items to be recovered.
- d. For previously established reserve accounts, a summary with supporting work papers showing over or undercollections in the reserve account.

Staff will prepare the necessary paperwork, i.e., the Advice Letter and Notice to Customers, and provide these documents to the utility. The utility is responsible for the distribution of the notice to its customers.

18. Class B and C utilities may submit two copies of a draft advice letter (proposal), including supporting work papers, to the staff for review (see Appendices B and D). Draft form simply means that the advice letter and the tariff sheets are not numbered, the advice letter is called a draft advice letter, and the date of publication (or distribution) of the Notice to Customers is not filled in. The advice letter must still be typed and all work papers must be legible and logically arranged. The purpose of a draft advice letter is to permit the branch to review the submittal for errors and to eliminate the possible need to reject or supplement a filed advice letter. Exceptions to the draft advice letter procedure will be permitted if, in staff's view, a utility is sophisticated enough to file a normal advice letter. Class A utilities shall submit a regular advice letter.

19. Class A, B and C water companies will provide the information in Appendix C, with all supporting work papers showing insurance recoveries, contracts, costs and calculations. Proof of the underlying expense change such as a copy of the invoice or notice of impending cost

¹⁷ Op. cit.

change must be included. Class A utilities will include a compact disk or floppy disk copy of all calculations, or e-mail the spreadsheets to water_division@cpuc.ca.gov.

D - PROCESSING THE ADVICE LETTERS

20. Expense offset rate increase advice letters should be processed within 30 days. If it becomes evident that the analysis won't be completed in time, the analyst must suspend the advice letter by informing the utility by letter prior to the 30th day stating why the advice letter is being suspended, inform the tariff unit so that the information can be published in the Commission Calendar, and inform his or her supervisor, who will inform the Branch Chief. Rate base offset and reserve or memorandum account recovery advice letters will require a resolution.

21. For all advice letters, the analyst will go through the work papers, verifying all calculations, and requesting additional information as necessary, to ensure that the request is just, reasonable and correct. All charges booked to memorandum accounts must be less than three years old unless the costs are fully justified for being older. Legal expense memorandum accounts cannot be recovered until the case is closed if the utility was the defendant. Legal expense memorandum accounts where the utility is the plaintiff may be recovered prior to closure of the case, subject to refund. After advice letter approval, the analyst or Senior prepares the resolution, if necessary.

22. For Class B, C and D utilities, after review of the draft advice letter, the staff member will advise the utility to file the final advice letter and to notify its customers of the requested rate increase by sending the utility a filled-in copy of the Cover Letter and the Notice of Proposed Rate Increase (Appendix D); a copy of the filled-out Additional Information sheets (Appendix E); and, if necessary, a corrected draft Advice Letter. The utility then files the advice letter as specified in General Order No. 96 and notices its customers. The engineer or analyst logs in all customer responses received and replies to them.

E - CALCULATING OFFSET RATE INCREASES

23. For CPI offsets, all existing rates amounts are multiplied by one plus the consumer price index for all urban consumers (CPI-U) increase for the previous year expressed as a decimal. The Water Advisory Branch will provide this information to all water utilities early in the calendar year by mail.

24. Calculate rate base (Appendix C-1) and expense offset revenue changes (Appendix C-2) by creating an offset summary of earnings (Appendix C-3). The allowable offsettable amount is added to ratebase or expenses. The depreciation expense is adjusted by multiplying the incremental plant in service by the last approved depreciation factor for the utility or district. The rate of return is that last approved for utility, or, for multi-district utilities, the last approved for the district, whichever is lower. For Class B utilities the rate of return is the last approved for the utility or district adjusted by the same number of basis points that class C and D rates of return have been adjusted over the same period of time. For Class C and D utilities, use the midpoint of the latest Class C and D returns published by the Water Division adjusted by any deviation to the rate of return made in the utility's last general rate case.

25. Expense offset rate increases are based on the Adopted Quantities¹⁸ from the last general rate case (GRC) or the Additional Information from the last offset processed. The last GRC proceeding should not be more than five years old. Normally, after five years, the utility no longer qualifies for an offset and must file for a GRC if it wants rates modified to account for cost changes. Exceptions to this procedure will be permitted if, in the view of the staff, unique circumstances exist that argue for continued processing of offset filings.

26. The Adopted Quantities are included as an Appendix to Commission decisions and resolutions for all general rate proceedings and the Additional Information (Appendix E) must be included as an attachment to the advice letter for all offsets. The utility may have to contact the tariff unit to obtain the Additional Information and unit costs to be used for an offset.

27. As stated earlier, an offset rate increase covers changes in costs since the last rate case or offset. For example, if the electric utility's rates are increased by two cents per kWh, a water utility can request a rate increase to offset the increased cost of purchased power. The following sample calculation for purchased power illustrates the procedure:

Adopted Quantities (last general rate proceeding)

- a. 1,500,000 kWhs at a unit cost of \$0.10 per kWh.
- b. 2,000,000 Ccf water sales.

New (current) cost of electrical power

\$0.12 per kWh

Increased expense

$$1,500,000 \text{ kWh} \times (\$0.12 - \$0.10/\text{kWh}) = \$30,000$$

The requested increase in revenue is \$30,000 and the requested change in rates (assuming the same incremental increase to the quantity rate) is:

$$\frac{\$30,000}{2,000,000 \text{ Ccf}} = \$0.015 \text{ per Ccf}$$

so the tariff sheets would be changed to reflect a quantity rate \$0.015 per Ccf higher than the last adopted rate.

28. Calculation Guidelines for Rate Changes. The following guidelines should be used for calculating the changes in rates.

- a. Water Production Expense Changes for a metered system -
Compute an incremental change in cents per Ccf by dividing the annual amount of the cost increase by the adopted annual sales adjusted for unaccounted-for water. Apply this increase to all blocks if multiple block rates still exist.
- b. Water Production Expense Changes for a flat rate system -
Compute an incremental change for the flat rate tariffs similar to the computation

¹⁸ Memorandum from Wesley Franklin to Hydraulic Branch – Supervisors and Seniors, Aug 31, 1983, Subject: Adopted Quantities

of a surcharge by dividing the annual amount to be amortized by the number of actual services and the number of billing periods per year. Adjust the surcharge by the same factors as the flat rate schedule itself (by lot size or service size).

- c. Non-Water Production Expenses - Compute an incremental change in the flat rate tariff similar to the computation above or in the service charge scaled by the capacity factor equivalents for different meter sizes for metered services.

33. The following rate design policy shall be used for offsets unless there is a valid cause for deviation¹⁹:

- a. No change of rate design (percentage of fixed costs in service charge for metered service) shall be made in an offset rate proceeding.
- b. Increases involving water systems that have both flat rate and metered customers should be allocated to those classes so that the metered customer who uses an average amount of water receives the same percentage increase as a flat rate customer.

F. – Means Test for Purchased Water, Purchased Power and Pump Tax Recovery

29. All Class A water company districts must file for reserve account recovery by advice letter annually. A separate reserve account calculation must be performed for each of the offsettable expense categories (purchased water, purchased power, pump tax) for the period January 1 through December 31. An earnings test based on a recorded basis must be performed for each district. If the district is over earning, the amount of over earning must be subtracted from the undercollection in the balancing accounts.

- a. If the undercollection, excluding over earning, if any, is more than 2% of the last authorized revenue requirement, the utility must request recovery of the undercollection through a surcharge.
- b. If the undercollection, excluding over earning, if any, is less than 2% of the last authorized revenue requirement, the Water Division will send a letter to the utility to include the approved balance in the next GRC or next annual filing.
- c. The approved balance (undercollection), plus interest for the next year, will be added to the next year balancing accounts balance after over earning, if any, is subtracted from the balance of the next year.
- d. If the balance shows overcollection of more than 2% of the last authorized revenue requirements, the utility must file to credit customers.
- e. If the overcollection, excluding over earning, if any, is less than 2% of the last authorized revenue requirements, the Water Division will send a letter to the utility to include the approved balance in the next GRC or next annual filing.

¹⁹ A change in rate design may require a formal proceeding. At a minimum there must be a substantive justification for the change. See *California Manufacturer's Association v. Public Utilities Commission* 24Cal.3d 251; 155 Cal.Rptr. 664, 595 P.2d 98.

30. Means Test: The recorded rate of return means test shall be used to evaluate earnings for revenue received for all years (See Appendix H). If a utility is outside of the rate case cycle but is not over earning according to the above tests, then it shall recover as set forth in Section 27 a. above. This scenario may occur if both the Commission and the utility agree to defer a utility's rate case filing pursuant to Pub. Util. Code § 455.2.

31. Amortization of Undercollection in the Reserve Account (Metered):

- a. Recovery of reserve account accruals related to water production expenses shall be recovered through a surcharge on the quantity rates for metered customers. Accruals related to non-water production expenses, such as ad valorem taxes, should be recovered through a surcharge on the service charge. If the fixed expense changes are a small percentage (less than 10%) of the variable expense changes, or if they would result in a small monthly surcharge (less than \$0.50) they may be lumped together, and a single surcharge applied to quantity rates.
- b. Surcredits shall apply to service charge only and be designed to return the money as soon as reasonably possible.
- c. Recovery shall be tracked in a balancing account.

32. Reserve and memorandum account amortization surcharges shall be spread over one year for undercollections of less than 5% of gross revenues, over two years for undercollections of 5% to 10% of gross revenues and over three years for undercollections over 10% of gross revenues. Recovery shall be tracked in a balancing account.

33. After the advice letter is approved, the Tariff Unit sends one copy to the utility. The utility can then charge the new, authorize rates for service after the effective date that is shown on the tariff sheets.

G - WEIGHTING FACTORS

34. Because the date of the change in the offsetable expense and the effective date of the new tariff rate may occur during the billing cycle, the utility must weight the new rates by the number of days in the billing cycle and the number of days that the utility may charge the new rate. For utilities that read meters daily the following formulas will be applied when calculating the customer's bill. Utilities that read all meters within a few days may use a straight proportion for calculating the weighting.

- a. Weighting Factors--Monthly Billing Cycle

Expense Weighting Factor

$$EW = (N_1 - E_e + 1)/N_1$$

Flat Rate or Service Charge Revenue Weighting Factor

$$FRW = (N_1 - E_r + 1)/N_1$$

Metered Revenue Weighting Factor

$$MRW_1 = (N_1 - E_r + 1)^2 / (2 \times N_1^2)$$

$$MRW_2 = 1 - [(E_r - 1)^2 / (2 \times N_1 \times N_2)]$$

b. Weighting Factors--Bimonthly Billing Cycle

Expense Weighting Factor

$$EW = (N_1 - E_e + 1) / N_1$$

Flat Rate or Service Charge Revenue Weighting Factor

$$FRW = (N_1 - E_r + 1) / N_1$$

Metered Revenue Weighting Factor

$$MRW_1 = (N_1 - E_r + 1)^2 / 2N_1 (N_1 + N_1^2)$$

$$MRW_2 = (2N_1 + N_2 - 2E_r + 2) / 2(N_1 + N_1^2)$$

$$MRW_3 = 1 - [(E_r + 1)^2 / 2 (N_1 + N_2)N_3]$$

Where:

E_d = Effective date of expense change

E_r = Effective date of revenue rate change

E_w = Expense weighting factor

FRW = Flat rate revenue weighting factor

$MRW_{1,2,3}$ = Metered revenue weighting factor for the first, second and third months

$N_{1,2,3}$ = Number of days in the first, second and third months.

H - NOTICE AND RESPONSES

35. Although expense offset advice letters do not have to be noticed to the customers²⁰, it is good public policy to do so. All advice letters shall use the notice language in Appendix C. The following procedure shall be used to notify the utility's customers:

- a. For an increase that results in a rate increase of greater than 10%, the utility shall distribute a notice to all of its customers.
- b. For an increase that results in a rate increase of 10% or less, the utility may publish a Notice to Customers in the Official Notice section of a local newspaper of general circulation.
- c. For a utility with a significant number of part-time customers or if located in an area not served by a local newspaper, the utility shall distribute a notice to all of its customers.
- d. For a decrease in rates (surcredit) no notice is required, but the utility should consider a bill insert explaining the refund if the expense if the insert is not too great.

36. Class B, C and D utilities should not distribute or publish the notice until the staff has reviewed it and informs the utility that it is acceptable. After the notice is distributed or

²⁰ Rules of Practice and Procedure of the California Public Utilities Commission, Rule 24.

published, these utilities can file the final Advice Letter. The customers then have 20 days from the date the Advice Letter is filed, or twenty days from when the notice is published, whichever is later, to file a protest (see next paragraph). The public can also send responses to the Commission concerning the rate increase.

37. Although letters from customers that complain about rate increases are sometimes called protests, they are not. A protest is defined in Rule 8.1 of the Commission Rules of Practice and Procedure and in G.O. 96, and must be served on the utility, and responded to by the utility within 5 days. Letters to the Commission that object to the advice letters, per G.O. 96, are called responses. Nevertheless these letters are important indicators of the ratepayer's attitude and must be answered immediately. If service or noncompliance is not an issue, the assigned staff shall reply to the customers using the form letter in Appendix F. However, if the customer's letter includes specific questions or complaints, the letter should be modified to include an informed response to each specific item (service, billing or other problems). Additionally, letters of this type should be forwarded to the Consumer Affairs Branch for logging-in (and possibly for handling).

38. In the case of serious service or compliance violations, the utility's rate increase should be made subject to refund until the utility files a plan that addresses the problems. In other instances, the Division Director will determine the appropriate course of action.

Appendix A
PROCEDURES FOR MAINTAINING RESERVE ACCOUNTS

1. PURPOSE

The purpose of a reserve account is to track the undercollection or overcollection associated with the incidence of an expense change and the authorization of revenue to offset the expense change.

2. APPLICABILITY

Pursuant to Section 792.5 of the Public Utilities Code, a reserve account is to be kept for all expense items for which revenue offsets have been authorized. A separate reserve account must be maintained for each offset expense item. All multi-district water utilities shall maintain separate reserve accounts for each district. Reserve accounts must be kept separate from the general ledger accounts of the utility.

3. START DATE

All water and sewer system utilities shall begin maintaining a reserve account by the procedure described herein as of July 1, 1983.

4. ADOPTED QUANTITIES

Test year customer, expense, investment and revenue projections found reasonable in the latest general rate case decision will be used for the procedures herein.

Reserve accounts maintained beyond the latest test year will use the latest adopted quantities. Those cases where adopted quantities do not exist or where the latest decision is older than five years will be handled on a case by case basis by the Commission staff.

5. EXPENSE COMPONENT

- a. Water Production Expenses – The expense component of the reserve account is given by:

$\text{Expense Component} = \text{Recorded Consumption} \times \text{Incremental Expense Rate Change}$

- b. Non-Water Production Expenses – The expense component of the reserve account is given by:

$\text{Expense Component} = \text{Adopted Expense} \times \text{Percent Expense Change}$

All expense components are to be booked monthly. In the case of non-water production expenses, it will be necessary to divide the annualized expense change by twelve (12).

Appendix A
PROCEDURES FOR MAINTAINING RESERVE ACCOUNTS

6. REVENUE COMPONENT

- a. Water Production Expenses – The revenue component of the reserve account is given by:

$$\text{Revenue Component} = \text{Recorded Water Sales} \times \text{Incremental Revenue Rate Change}$$

- b. Non Water Production Expenses – The revenue component of the reserve account is given by:

$$\text{Revenue Component} = \text{Recorded Meter Equivalent Customers} \times \text{Incremental Revenue Rate Change}$$

7. RESERVE ACCOUNT BOOKING PROCEDURE

Entries shall be made to each individual reserve account at the end of each month as follows:

Water Production Expenses

- a. If positive a debit entry, if negative a credit entry, equal to the expense component as calculated in Section 5.
- b. If positive a credit entry, if negative a debit entry, equal to the revenue component as calculated in Section 6.
- c. The monthly reserve account accrual is the difference between 7a. and 7b.
- d. The balance shall be adjusted by multiplying by one plus one-twelfth of that month's 90-day commercial paper rate.

The utility shall file an advice letter contain the following workpapers as shown below:

Appendix A
PROCEDURES FOR MAINTAINING RESERVE ACCOUNTS

EXAMPLE MEMORANDUM ACCOUNT LANGUAGE FOR THE PRELIMINARY STATEMENT

G. CATASTROPHIC EVENT MEMORANDUM ACCOUNT (CEMA):

1. PURPOSE: The purpose of the CEMA is to recover the costs associated with the restoration of service and Any Water Co. facilities affected by a catastrophic event declared a disaster or state of emergency by competent federal or state authorities. The balance in the CEMA will be recovered in rates after CPUC review and audit of the recorded CEMA balance. The authority to establish this account was granted in CPUC Resolution E-3238, dated July 24, 1991 and Public Utilities Code Section 454.9.

Should a disaster occur, Any Water Co. will inform the Executive Director of the CPUC by letter within 30 days after the catastrophic event that Any Water Co. has started booking costs in the CEMA.

2. ACCOUNTING PROCEDURE: Any Water Company (AWC) may maintain a memorandum account for its expenses and other recovery/reimbursements in connection with a catastrophic event as defined in Section 454.9. These expenses must be additional or incremental to those allowed in AWC's last general rate case proceeding. AWC shall make entries to this account at the end of each month as follows:

- a. Debit entries equal to the incremental or additional amounts recorded in AWC's operations and maintenance and administrative and general expense accounts that were incurred as a result of the catastrophe.
- b. Debit entries equal to the depreciation and/or amortization amounts of new or replacement utility plant installed to continue the provision of uninterrupted services to customers.
- c. Debit entries equal to the return on investment on the average monthly balance of new or replacement utility plant installed in (b) above.
- d. Credit entries equal to the proceeds reimbursed by the utility's insurance covering such events.
- e. Credit or debit entries to transfer all or a portion of the balance in this memorandum account to other adjustment clauses for future rate recovery, as may be approved by the Commission.

In addition, the water utility shall file an advice letter to the Commission detailing any utility plant retired from service and the proposed rate making treatment for such plant.

Appendix C
EXAMPLE CALCULATIONS FOR OFFSETS

Any Water Company
Rate Base Offset

Computation of Well Cost

Engineering	20,000
Backhoe Service	6,000
Rock	5,000
Well Cost	500,000
Capitalized Interest	<u>10,000</u>
Total	541,000

Cost of New Construction

Land Acquisition	50,000
Geological Reports	40,000
Cost of Well	<u>541,000</u>
Total Additions	631,000

Depreciation Rate 3%

Annual Depreciation 18,930

Property Taxes @ 1% 6,310

Cost of Offset Filing 1,200
(\$3,600 amortized over three years)

Return Calculation

Rate Base Increase	631,000
Allowed ROR	10%
Return	63,100

Revenue Requirement Increase

Revenue Increment 63,100

Depreciation	18,930
Property Taxes	6,310
Prep Cost	1,200
Income Taxes	<u>14,959</u>

Annual Revenue
Requirement Increase 104,499

Appendix C
EXAMPLE CALCULATIONS FOR OFFSETS

Income Tax Calculations

Revenue Increment Subject to Income Tax	63,100
State Tax at 8.84%	5,578
Net subj. to Fed. Tax	57,522
1 st 50,000 at 15%	<u>7,500</u>
Remaining	7,522
Next 25,000 at 25%	1,881
Total Fed. Tax	9,381
State Tax	<u>5,578</u>
Total Income Tax	14,959

Proof of Income Tax Calculations

	Per Res. W-XXXX	Requested this Offset
Revenues	989,135	1,093,634
Operating Expenses	720,478	746,918

Appendix C
EXAMPLE CALCULATIONS FOR EXPENSE OFFSETS

Advice Letter No. 26

SUMMARY OF EARNINGS - TEST YEAR 1999
(\$000)

<u>Item</u>	<u>Rates Authorized by D.99-01-001</u>	<u>Increases</u>	<u>At Proposed Rates</u>
<u>Operating Revenues</u>			
General Metered Service	\$ 6,950.2	\$ 285.7	\$ 7235.9
<u>Operating Expenses</u>			
Payroll	1,530.8	0	1530.8
Purchased Power	1,200.6	280.1	1450.5
Purchased Water	0.0	0.0	0.0
Uncollectables	123.0	5.6	128.6
Depreciation	355.0	0.45	355.45
Payroll Tax	510.9	0	510.9
Taxes - Income	<u>1,040.8</u>	<u>0</u>	<u>1040.8</u>
Total Expenses	5,755.5	280.55	6,036.0
Net Operating Revenue	1,540.7	0	1,549.9
Average Plant	181,733.0	20.0	181,753.0
Average Depreciation Reserve	6,309.0	1.3	6,310.3
Net Plant	175,424.0	18.7	175,442.7
Less: Adv. & Contributions	70,383.0	0	7,038.0
Rate Base	105,041.0	18.7	105,059.7
Rate of Return	11.00%	11.00%	11.00%

Appendix C
EXAMPLE ACCEPTANCE LETTER AND NOTICE OF PROPOSED OFFSET RATE INCREASE
FILING

Date

Mr./Ms. Owner

Any Water Company

Address

City, State ZIP

Dear Mr./Ms. Owner:

This is to acknowledge receipt of your draft offset advice letter rate increase request dated _____. The Water Branch has completed its preliminary review of your submittal and finds it complete for filing as of today.

In order to promote greater ratepayer awareness during the rate increase process and to avoid later claims of lack of due process, we require that you provide notice of this increase to afford customers the opportunity to be heard and to ask questions about the proposed increase and the approval process. Please date, fill in the blanks and distribute the enclosed notice.

Since the increase is for less than 10% of your latest recorded gross revenues, please arrange to have the enclosed notice published in the Official Notice section of a newspaper of general circulation in your service territory.

or

Since the requested increase is for more than 10% of your latest recorded gross revenues, please distribute the enclosed Notice to each customer. This may be distributed by mail or otherwise, but should be distributed as soon as possible.

You should also distribute a sufficient number of copies to your customers who submeter others and request that they make a distribution to their submetered users. Please furnish the Commission with a copy of the notice as distributed by enclosing a copy with the four copies of the Advice Letter that you are now authorized to file. Please advise us of the date of such distribution and whether by mail or otherwise.

The Branch will evaluate any letters received from the utility's customers and will correspond with you regarding further processing of your request for an increase in rates.

If you have any further questions, please call me at (415) 703-____. I appreciate your cooperation in this matter.

Very truly yours,

Your name, Your classification

Water Branch

Water Division

Enclosure

bcc: FLC

Appendix C
EXAMPLE ACCEPTANCE LETTER AND NOTICE OF PROPOSED OFFSET RATE INCREASE
FILING

Date

NOTICE OF PROPOSED RATE INCREASE BY ANY WATER COMPANY

Any Water Company is requesting that the California Public Utilities Commission (CPUC) increase its gross revenue by \$280,100, or 4% to offset purchased power increases from Southern California Edison Co. and to recover increased water testing costs.

The revenue increase will recover only the added costs discussed above. This increase will not increase Any Water Company's profits.

The present rates have been in effect since January 1, 1999.

A comparison of the rates now authorized and the rates proposed follows:

General Metered Service:

Service Charge:

	Per Meter Per Month	
	Present Rates	Proposed Rates
For 5/8 x 3/4-inch meter.	\$ 15.50	\$ 15.70
For 3/4-inch meter.	\$ 16.05	\$ 16.30
For 1-inch meter.	\$ 18.25	\$ 18.60
For 1-1/2-inch meter.	\$ 21.00	\$ 21.45
For 2-inch meter.	\$ 24.85	\$ 25.45

Quantity Rate:

All Water, per 100 cu. ft.	\$ 1.58	\$ 1.60
------------------------------------	---------	---------

Reserve Account Amortization surcharge:

All Water sold, per 100 cu. ft.	\$ 0.149	\$ 0.164
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Protests and Responses

There are two ways to respond to this notice. You can send a protest to the CPUC and the utility, or you can send a response to the CPUC, with a copy to the utility if you wish.

A protest is a document objecting to the granting in whole or in part of the authority sought in this advice letter.

A protest must be mailed within 20 days of the date the California Public Utilities Commission accepts the advice letter for filing. It must state the facts constituting the grounds for the protest, the effect that approval of the advice letter might have on the protestant, and the reasons the protestant believes the advice letter, or a part of it, is not justified. If

Appendix C
EXAMPLE ACCEPTANCE LETTER AND NOTICE OF PROPOSED OFFSET RATE INCREASE
FILING

the protest requests an evidentiary hearing, the protest must state the facts the protestant would present at an evidentiary hearing to support its request for whole or partial denial of the advice letter. The utility must respond to a protest within five days.

A response is a document that does not object to the authority sought, but nevertheless presents information that the party tendering the response believes would be useful to the Commission in acting on the request.

All protests and responses should be sent to:

California Public Utilities Commission, Water Division
505 Van Ness Avenue
San Francisco CA 94102
Fax: (415) 703-4426
E-Mail: water_division@cpuc.ca.gov.

All protests should be sent to this utility to

_____, _____,
(name) (address)

_____, _____.
(fax number) (e-mail address)

If you have not received a reply to your protest from the utility within 10 business days, contact this person at

_____.
(phone)

WORKPAPERS FOR ADVICE LETTER NO. 26

Rate of Return (Rate Base offsets, CPI offsets and memorandum account recovery only)

1. The recorded rate of return on rate base for the 12 months ending September 1999 is 9.8%.

(Class A utilities only)

2. The recorded weather-normalized rate of return on rate base for the 12 months ending September 1999 is _____.

The weather normalized rate of return is calculated by calculating revenues by multiplying the adopted consumption per customer by the actual number of customers, subtracting the adopted expenses and associated taxes and fees and applying the net revenues to the actual rate base.

Purchased Power

Decision (D.)98-01-001 included Any Water Company rates effective October 1, 1999 of \$0.14932/kWh on adopted usage of 2,445,200 kWh. Copies of the Adopted Quantities Tables from D.99-01-001 are attached.

Increases in SCE rates of 0.01018/kWh became effective October 1, 1998. A copy of this tariff (or a bill with the new rate circled) is attached.

Increase in purchased power costs of 24,450,200 kWh x \$0.01018/kWh = \$240,900.

Ad Valorem taxes have been increased by 0.12% to fund a new school. A copy of the approved county resolution is attached.

Summary of Increased Expenses

Purchased Power	\$240,900
Ad Valorem Taxes	30,200

Required Rate Increase

$$\frac{\$280,100}{\$6,950,200} = 4.04\%$$

Computation of Rates

Apply purchased power increase to quantity rates and ad valorem increase to service charge rates.

Appendix D
EXAMPLE WORKPAPERS

Purchased Power - Quantity Rates

D.99-01-001 included adopted water sales of:

Block 1	0 - 3 Ccf	1,850,160 Ccf
Block 2	Over 3 Ccf	<u>14,560,400 Ccf</u>
		16,410,560 Ccf

Increase in quantity rates - use same cents/Ccf increase for all water sales:

$$\frac{\$240,900}{16,410,560 \text{ Ccf}} = \$0.0152/\text{Ccf}$$

Ad Valorem Tax - Service Charge Rates

D.99-01-001 included adopted customers services of:

5/8 inch meter	50,421
2 inch meter	<u>500</u>
Total	50,921

Total Equivalent 5/8 x 3/4" meters

$$\frac{2" \text{ rate}}{5/8" \times 3/4" \text{ rate}} = \frac{\$50.00}{20.25} = 2.222$$

Total Equivalents

$$50,921 + (500 \times 2.222) = 50,421 + 1,111 = 51,532$$

\$ per meter/year for \$3,200 increase

$$\$3,200/51,532 = \$0.0587/\text{meter/year}$$

\$ per meter/month

$$\$0.0587/12 = \$0.482/\text{meter/month}$$

Let 5/8 x 3/4 increase by 5 cents

$$\text{Then } 2" = 0.0482 \times 2.222 = \$0.1071 \text{ or } 10 \text{ cents}$$

Check revenues against increase

$$\begin{array}{r} 5,421 \times 0.05 \times 12 = \$3,253 \\ 50 \times 0.10 \times 12 = \underline{\$60} \\ \$3,313 \end{array}$$

\$3,313 revenue

3,200 increase

\$ 113 overcollection

Reserve Account Undercollection

The reserve account balance as of September 30, 1999 was \$5,100. Since this is less than 2% of gross revenues, no recovery is requested.

Workpapers for Reserve Account Recovery

WORKPAPERS

All workpapers will have

1. a table of contents,
2. page numbering, and
3. cross references to numbers in the workpapers.

The page number will be in the form Section – Part – page number.

Section One: Summary

Part A. Summary sheet: provide for each district for each calendar year:

- (a) the revenues, expenses and balance for each of the balancing accounts for purchased water, purchased power, pump tax from Section Two Part E;
- (b) total over earnings as a result of earnings test from Section Three, Part C.2.d;
- (c) amount of over earnings allowed to be returned to the customers from Section Three Part C.3;
- (d) net under collection or over collection from Section Four, Part A;
- (e) reported under collection from Section Four, Part B;
- (f) requested recovery of net under collection from Section Four, Part B;
- (g) duration of surcharge as related to requested recovery of under collection from Section Four, Part B;
- (h) requested customer refunds of over collection from Section Four, Part C;
- (i) duration of surcredit as relates to the refund of over collection from Section Four, Part C .

If any of the items above are zero, indicate as such.

In addition, on the same Summary sheet, provide the balance in each of the non-supply expense memorandum accounts for each calendar year for each district.

Section Two: Balancing Account Calculations and Supporting Documents For Table 1

Appendix D
EXAMPLE WORKPAPERS

PART A. The amount in the balance for supply expense reserve accounts will be calculated exactly in the same fashion as calculated in Table 1A and 1B. A Table 1 will be calculated for each supply expense for each district for each calendar year.

1. The recorded sales in column b of Table 1 will be provided for each month and total recorded sales for each year will be verified by providing a copy of the relevant page in the annual report.
2. The recorded power consumption or pumped water or purchased water in column c of Table 1 will be supported by providing sales documentation verifying the figures in column c. The documentation will be in the form of actual bills for purchased water and pump tax or a spreadsheet for purchased power.

Part B. Calculations of expense rate change for purchased power, purchased water and pump tax in column d of Table 1 will be provided in the following manner: (a) the actual model used to derive the authorized expense rate; (b) the new expense rate based on exactly the same model used to derive the authorized expense rate in step (a); and (c) the difference between step (a) and (b) will be the “incremental expense rate change” shown in column d of Table 1 of this workpaper which must be constant for the period between rate changes. Provide related documents verifying the new expense rate.

If the request includes purchased power recovery, include in this section a complete description of the calculation of the incremental composite rate based on calculation method included in a letter from Fred L. Curry of the Water Division, dated February 27, 2002 (Attachment A) including the adopted quantities from the last GRC or justification for other method if composite rate information from the last GRC is not available. The incremental composite rate must be a constant for the period between rate changes (same cents per kilowatt hour). Methods that result in differing amounts per month in column d in Table 1 will be rejected.

PART C. If an offset advice letter was filed during the year, verify incremental revenue rate change in column e of Table 1 by including a copy of the Commission resolution authorizing the incremental rate change. If no offset advice letter was filed, the incremental revenue rate change will be zero.

PART D. Verify the commercial paper rate by including a copy of the summary of the historical values of the commercial paper rates for the year obtained from Federal Reserve’s web site.

.....

Do the same calculations for each of other reserve accounts in the district. The balance in each of the reserve accounts will be either under collection or over collection and very seldom zero. Under collection will be shown as negative number and over collection as positive number. **Do not report** over collection in parenthesis.

Appendix D
EXAMPLE WORKPAPERS

Part E. Show the under or over collection for purchased water, purchased power and pump tax and the total balance for the three accounts. If there is no balance for any of the three accounts, indicate zero.

Appendix D EXAMPLE WORKPAPERS

Table 1A: Purchased Power

(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)	(k)	(l)	(m)
		Recorded	Incr. Exp.	Incr. Rev.	Rev. Comp.	Rev Component with Interest	Exp. Comp.	Exp. Component with Interest	Over/(Under)	Comm'l. Paper	Int. Prev.	Accr. Prev.
			Rate Change	Rate Change	(b) x (e)	(f) + prev(g) + interest on prev (g)	(c) x (d)	(h) + prev(i) + interest on prev (i)	(h) - (f)	Rate	(j) + prev (m) + (l)	(k) + (h) + (j)
2003	Recorded Sales (KCcf)	Power Cons.(Kwh)	(\$/Kwh (see handout #7)	(\$/Ccf (from Offset Adv. Ltr.))	(\$)	(\$)	(\$)	(\$)	(\$)	(%)	(\$)	(\$)
Month												
Jan	240.2	168,600								4.77	0.00	0.00
Feb	237.3	165,600								4.79	0.00	0.00
Mar	234.2	162,400	0.015				2436	\$2,436.00	-2436	4.81	0.00	(2436.00)
Apr	247.2	178,400	0.015	0.0111	2743.92	\$2,743.92	2676	\$5,121.72	67.92	4.79	(9.72)	(2377.80)
May	328.6	231,000	0.015	0.0111	3647.46	\$6,402.38	3465	\$8,607.25	182.46	4.81	(9.53)	(2204.87)
Jun	328.4	235,000	0.025	0.0111	3645.24	\$10,074.19	5875	\$14,517.97	-2229.76	4.98	(9.15)	(4443.78)
Jul	349.3	242,200	0.025	0.0111	3877.23	\$13,994.32	6055	\$20,634.80	-2177.77	5.11	(18.92)	(6640.48)
Aug	342.8	247,000	0.025	0.0193	6616.04	\$20,671.58	6175	\$26,900.07	441.04	5.25	(29.05)	(6228.49)
Sep	333.2	231,100	0.030	0.0193	6430.76	\$27,193.99	6933	\$33,952.33	-502.24	5.32	(27.61)	(6758.34)
Oct	298.0	206,600	0.030	0.0193	5751.4	\$33,078.64	6198	\$40,316.70	-446.6	5.88	(33.12)	(7238.06)
Nov	247.3	180,000	0.030	0.0193	4772.89	\$38,011.68	5400	\$45,911.90	-627.11	5.81	(35.04)	(7900.21)
Dec	207.6	150,000	0.030	0.0193	4006.68	\$42,204.30	4500	\$50,636.48	-493.32	5.87	(38.65)	(8432.18)
						\$42,204.30		\$50,636.48				
Total Revenue Component					41491.62							
	Total Expense Component							49713				
		Total Incremental Expense, Revenues w/ Interest									(8432.18)	

Facts:

1. Increase in power costs in March 2003.
2. Granted offset rate increase in April 2003.
3. Additional increases in power costs and additional offsets.
4. Over earnings of \$36,000 (See Appendix B, Page 3 of handout #2, D.03-06-072).
5. Purchased Power Expense Account is \$49,713.

Section Three: Earnings Test and Supporting Documents For Tables 2 and 3

Part A. Include Table 2 in this part. Table 2 must include three columns:

- (a) "Decision": 1st column- identical numbers for the line items as appeared in the decision;
- (b) "Recorded": 2nd column – recorded figures for the line items included in the decision and
- (c) "recorded with adjustments": 3rd column- recorded figure with adjustments. These adjustments must include: (1) total revenue and expense components calculated in columns f and g shown in Table 1; and (2) surcharges and sucredits, if any. If there are no surcharges or sucredits, indicate zero for each item. In addition, the adjustments will include extraordinary revenues and expenses, if any. **Table 2 must be provided for each district for each year.**

Part B. Use the pages in this Part to identify and verify the source of each number in the "Recorded" and the "Recorded With Adjustments" columns in Table 2 and clearly annotate each line on the table to identify that page. Clear handwritten annotations are acceptable. On the supporting page, annotate the number that is being referred to by this table. If the number is a combination of amounts from the annual report, include those pages and explain how the calculation was made. If the amount deviates from that in the annual report, explain the deviation.

If the amount had to be calculated by the utility analyst, include a copy of the information the analyst used and the analyst's calculation.

Part C. (1) If the recorded rate of return in the "Recorded with Adjustments" column in Table 2 is less than the authorized rate of return, proceed to Section Four. If the recorded rate of return in the "Recorded With Adjustments" column exceeds the adopted rate of return, calculate the amount of the over earnings as shown at the bottom of Table 2.

(2) To obtain the interest on the amount of over earnings, follow the calculations exactly in the same fashion shown in Table 3: (a) distribute the amount of over earning to each month of the year equally by dividing the amount by twelve; (b) assign the commercial paper rates for each month from the Federal Reserve web-site; (c) obtain interest for each month; and (d) Obtain total over-earning, including interest.

(3) The amount of over earnings, including interest, will have to be credited to the customers, partially or fully, depending on the amounts of total expense component, including interest, and revenues, including interest. In examples in Tables 2 and 3, the accrual in the account consists of three components: the incremental expenses, the incremental revenues, and adjustment to incremental revenues, all with interest.

Appendix D
EXAMPLE WORKPAPERS

When the incremental purchased power expense \$49,713 plus interest, which equals (\$50,636) and incremental purchased water expense \$3,779, which equals (\$3,860), are reduced by the amount of earnings plus interest, \$36,909, the balance of offset expenses not reduced by the over earnings is \$17,587 ($\$50,636 + \$3,860 - \$36,909 = \$17,587$). When the sum of offset revenues of \$41,492, plus interest, which equals to \$42,204 and \$1,024, plus interest, which equals to \$1,044, are applied to the \$17,587 that was **not** reduced by over earning, it leaves us with a balance of \$25,662 ($\$42,204 + \$1,044 - \$17,585 = \$25,662$), which will be credited to the customers. If the over earnings plus interest were, for example, \$200,000 instead of \$36,909, in this case, the customers will not be charged the amount of expense components, including interest (\$54,496) and will be refunded the offset revenues, including interest, which is \$43,249.

Section Four: Surcharges or Refunds

Part A. Calculate net under collection or over collection in accounts by calculating sum of: (a) all the balances in the balancing accounts; and (b) over earnings used to adjust the balances in the accounts, if any. Over collections are designated as positive and under collection as negative (shown in a parenthesis).

Part B. Under collection-Report on or request recovery of net under collection in the accounts by amortizing the under collection and applying a surcharge to the quantity rates for the metered customers. For flat rate customers, the surcharge should be applied to individual lots, based on equivalent lot size. If the under collection is less than 2% of the last authorized revenue requirements, it will be reported, but no recovery will be allowed. If the amount is more than 2% but less than 5%, of the last authorized revenue requirements, recovery should occur in one year, for 5%-10% in two years and over 10% in three years.

Part C. Over collection-Request recovery of a net over collection by amortizing the over collection and crediting the service charge of all customers, based on the meter equivalent size of the service connection. For flat rate customers, the surcredits will be applied to individual lots, based on equivalent values in Flat Rate Tariff Schedule. Refunding will occur as soon as reasonably possible.

Appendix D
EXAMPLE WORKPAPERS

Table 2

SUMMARY OF EARNINGS

	Dollars in Thousands		
	Decision 00-00-000	- 2003 Recorded	2003 Recorded with Adjustments
OPERATING REVENUES			
Metered Revenues	2,209.0	2,509.3	2,509.3
Fire Service	20.5	20.9	20.9
Other	6.2	6.0	6.0
Adjustments:			
Purchased Power Surcharge			-41.5
Memorandum Account Amortization			-128.3
Total	2,235.7	2,536.2	2,366.4
OPERATING EXPENSES			
Purchased Water	408.2	439.2	439.2
Purchased Power	319.1	331.2	331.2
Chemicals	15.2	16.3	16.3
Payroll	307.5	301.2	301.2
Uncollectibles	8.2	8.6	8.6
Other O&M	155.2	169.0	169.0
Other A&G, & Misc	231.8	237.6	237.6
Adjustments:			
Pur Power Exp Component			-49.7
Subtotal	1,445.2	1,486.6	1,436.9
General Office Allocation	206.5	212.5	212.5
Total O & M Expenses	1,651.7	1,699.1	1,649.4
Depreciation	161.2	168.9	168.9
Ad Valorem Taxes	42.5	43.0	43.0
Payroll Taxes	34.2	33.9	33.9
Other Taxes and Fees	21.3	22.5	22.5
Subtotal	259.2	268.3	268.3
Total Operating Expenses	1,910.9	1,967.4	1,917.7
Net Revenues Before Income Tax	324.8	568.8	448.7
State Income Tax	15.6	27.3	26.8
Federal Income Tax	100.7	176.3	173.1
Total Income Tax	116.3	203.6	199.9
NET OPERATING REVENUE	208.5	365.2	248.8
RATE BASE	2,342.7	2,392.0	2,392.0
RATE OF RETURN:			
Authorized	8.90%		
Recorded		15.27%	10.4%

Over earning is 10.4%-8.90%=1.5%. The dollar amount of over earning is
1.5% x \$2,392,000 = \$36,000.

Appendix D
EXAMPLE WORKPAPERS

Table 3

Month	Adjustment (\$)	Commercial Paper Rate (%)	Interest (\$)	Accrual (\$)
Jan-03	3,000	4.77	-	3,000
Feb-03	3,000	4.79	12	6,012
Mar-03	3,000	4.81	24	9,036
Apr-03	3,000	4.79	36	12,072
May-03	3,000	4.81	48	15,121
Jun-03	3,000	4.98	63	18,183
Jul-03	3,000	5.11	77	21,261
Aug-03	3,000	5.25	93	24,354
Sep-03	3,000	5.32	108	27,462
Oct-03	3,000	5.88	135	30,596
Nov-03	3,000	5.81	148	33,744
Dec-03	3,000	5.87	165	36,909

Appendix D
EXAMPLE WORKPAPERS
CHECK-LIST OF ITEMS REQUIRED

Summary

1. Summary sheet in accordance with Section One, Part A of the workpapers

Balancing Account Calculations

2. Table 1
3. Calculations of balances in the balancing accounts for purchased water, purchased water and pump tax precisely in the same fashion as shown in Table 1 in the workpapers.
4. Verification of values of “recorded sales” in column b of Table 1 based on Section two, Part A.1 of the Workpapers.
5. Verification of values of “recorded consumption” in column c of Table 1 based on Section two, Part A.2 of the workpapers.
6. Verification of values of “incremental expense rate change” in column d of Table 1 based on Section Two, Part B of the Workpapers.
7. Verification of values of “incremental revenue rate change “ in column e of Table 1 based on Section Two, Part C of the workpapers.
8. Verification of values of “commercial paper rate” in column i of Table 1 based on Section 2 of Part D of the workpapers.
9. Calculations of net under collection or net over collection in the “Balancing-Type Memorandum Account” in accordance with Section Two, Part E. of the workpapers.

Earnings Test

10. Table 2
11. Provide Tables 2 in accordance with Section Three, Part A of the Workpapers.
12. Identification, verification and supporting documentation related to values in Table 2 in accordance with Section Three, Part B of the Workpapers.
13. Table 3, if applicable.
14. Provide table 3 in accordance with Section Three, Part C. 2. of the workpapers
15. Calculations of over earnings, if any, in accordance with Section Three, Part C.3 of the Workpapers

Surcharge or Refunds

16. Calculations of net over-collection or net under collection after over earnings, if applicable, in accordance with Section Four, Part A. of the Workpapers.

17. Calculations of the percentage of net under collection after over earning, if applicable, to authorized revenues.

18. Calculations of surcharge, if applicable, in accordance with Section Four, Part B of the Workpapers.

19. Duration of surcharge, if applicable, in accordance with Section 4, Part B of the workpapers

20. Calculations of surcredit in accordance with Section Four, Part C of the Workpapers

Appendix E
LETTER TO UTILITY AFTER DRAFT REVIEW

Meeting Date _____

Resolution W-_____

ADDITIONAL INFORMATION

ADVICE LETTER NO: _____

UTILITY: _____

DISTRICT: _____

I. RATE OF RETURN (Rate Base offsets, CPI offsets and memorandum account recovery only)

1. The recorded rate of return on rate base for the 12 months ending _____ is ____%.
2. The recorded pro-forma rate of return on rate base for the 12 months ending _____ is ____%.

Note: For Class A and B water companies, the recorded rate of return should be relatively easy to obtain. This return should be the latest reasonably available. For Class C and D water companies, the recorded rate of return may be difficult to obtain. However, the engineer should be satisfied that the utility is not over earning.

The pro-forma (or ratemaking) rate of return differs from the recorded rate of return in that the revenues and expenses are normalized for weather. In addition, the pro-forma return reflects the most current expense and tariff rate changes in effect. For Classes B, C and D the pro-forma will not be required.

Appendix E
LETTER TO UTILITY AFTER DRAFT REVIEW

II. INCREASE REQUESTED BY THIS ADVICE LETTER

<u>No.</u>	<u>Offset Items</u>	<u>Schedule No.</u>	<u>Amount</u>	<u>Date Effective</u>
1.	Purchased Power			
	_____	_____	\$ _____	_____
	_____	_____	\$ _____	_____
	Total		\$ _____	_____
2.	Purchased Water			
	_____	_____	\$ _____	_____
	_____	_____	\$ _____	_____
3.	Ground Water Charge			
	_____	_____	\$ _____	_____
	_____	_____	\$ _____	_____
4.	Amortization of Bal. Acct.			
	_____	_____	\$ _____	_____
	_____	_____	\$ _____	_____
5.	Uncollectibles & Franch. Tax			
	Uncollectibles		_____	Concurrent
	Franchise Tax		_____	Concurrent
	TOTAL Expense Offset		\$ _____	
	Reserve Account Status	Balance		As of
	_____	\$ _____		_____

Comments:

Reserve account is ____% of gross revenues. [This amount is too small to be amortized (<2%). This amount should be amortized over a 12-month period (2% to 5%). This should be amortized over a 24-month period (5% to 10%). This amount should be amortized over a 36-month period (>10%).]

Appendix E
LETTER TO UTILITY AFTER DRAFT REVIEW

III. CUSTOMER SERVICE

The utility serves approximately _____ customers within the system. A summary of customer complaints received at the Commission for the past 12 months is listed below. This summary relates to both formal and informal complaints. Complaint information is obtained from the formal files, Consumer Affairs Branch and also includes any letters received by the Water Advisory Branch complaining of service. This includes letters protesting the offset requests where service problems are mentioned.

<u>Complaint</u>	<u>Number</u>
Service	_____
Amount of bill	_____
Pressure Leaks	_____
Company Practice and Rules	_____
Miscellaneous	_____
Total	_____

Comments: (discuss complaint status and plan to resolve)

AWC investigates complaints in a timely manner and resolves them to the satisfaction of the customer in almost all cases.

IV. PUMP EFFICIENCIES (not necessary for offsets not related to pumping)

Pump efficiency tests were submitted by the utility as required; the rating of the _____ pumps checked are as follows:

<u>No. of Pumps</u>	<u>Qualitative Rating</u>
_____	Excellent
_____	Good
_____	Fair
_____	Low
_____	<u>Not Tested</u>
_____	Total

Comments: (discuss utility's plans for pumps rated low or not tested)

Appendix E
LETTER TO UTILITY AFTER DRAFT REVIEW

V. WATER CONSERVATION

Comments:

Appendix G
LETTER TO CUSTOMER

Letterhead

Date

Name

Address

City, St ZIP

Dear (Mr./Ms.) _____ Name _____:

I am replying to your recent letter of _____ concerning Any Water Company's Notice of Rate Increase.

The Commission staff is now in the process of thoroughly reviewing Any Water Company's request for this offset rate increase. The purpose of this type of increase is to permit a utility to recover, on a dollar-for-dollar basis, increases in (power, water, etc.) costs that are beyond its control. Commission procedures in authorizing offset increases ensure that the utility receives no profit from the increase.

Thank you for your time and concern.

Very truly yours,

_____, (Analyst, Utilities Engineer)
Water Advisory Branch
Water Division

Appendix G
PROCEDURES FOR MAINTAINING RESERVE ACCOUNTS

Letterhead if available

Advice Letter No. 26 Any Water Company (U 456 W) November 5, 1992

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ANY WATER COMPANY, requests ministerial review and approval of the following changes in tariff sheets applicable to _____.
(District)

C.P.U.C. Sheet No.	Title of Sheet	Canceling C.P.U.C. Sheet No.
119-W	Schedule No. 1, General Metered Service	106-W
120-W	Table of Contents	117-W

The effective date of the tariff schedule is requested to be _____.

Notice has been provided as required by GO 96. The Service List is attached to this Advice Letter (or) This advice letter was served on the same parties a Advice Letter (or Decision) #_____, dated _____.

The purpose of this advice letter is to include in rates the following increases in costs: (list increases by source, date and amount.)

(Justification for DHS Offset)

Assembly Bill 2995, in adding Section 4019.10 to the California Health and Safety Code (now section 116590 and 116595), directs the Department of Health Services (DHS) and local primacy agencies to charge the utilities within its jurisdiction for all operating costs. The legislation also authorized these costs to be passed on to those utilities' customers. Commission Resolution W-4327, dated March 6, 2002, authorizes any Class B, C and D water company to file the attached rate schedules, and to concurrently withdraw and cancel its present schedules for such service.

Any Water Company, Inc. had duly established the required memorandum account and recorded therein the amount of \$_____ representing expenses for DHS or the local primacy agency paid by the company.

Any Water Company, Inc. requests permission to recover the above charges from its _____ customers by adding an annual one time surcharge of \$_____ to each customer's bill. Workpapers justifying this charge have been provided to the CPUC Water Branch Staff.

There have been no other compensating changes in the company's revenues, remaining operating expenses or rate base that would offset the impact on earnings of these increases.

The Company's present General Metered Service rates became effective January 1, 1999, pursuant to Decision (D.) 99-01-001, in Application (A.) 98-06-001.

It has been determined that a 4.0% increase in gross revenues amounting to \$280,100 is required to offset the increased expenses.

The Commission staff has been provided with supporting workpapers showing the derivation of these quantities.

Appendix G
PROCEDURES FOR MAINTAINING RESERVE ACCOUNTS

The actions requested in this advice letter are not now the subject of any formal filings with the California Public Utilities Commission, including a formal complaint, nor action in any court of law.

Protests and Responses

A protest is a document objecting to the granting in whole or in part of the authority sought in this advice letter. A response is a document that does not object to the authority sought, but nevertheless presents information that the party tendering the response believes would be useful to the Commission in acting on the request.

A protest must be mailed within 20 days of the date the California Public Utilities Commission approves this advice letter for filing. It must state the facts constituting the grounds for the protest, the effect that approval of the advice letter might have on the protestant, and the reasons the protestant believes the advice letter, or a part of it, is not justified. If the protest requests an evidentiary hearing, the protest must state the facts the protestant would present at an evidentiary hearing to support its request for whole or partial denial of the application.

All protests or responses to this filing should be sent to:

California Public Utilities Commission, Water Division
505 Van Ness Avenue
San Francisco CA 94102
Fax: (415) 703-4426
E-Mail: water_division@cpuc.ca.gov,

and to this utility to _____, _____,
(name) (address)
_____, _____.
(fax number) (e-mail address)

If you have not received a reply to your protest within 10 business days, contact this person at _____.
(phone)

Appendix H
RECORDED MEANS TEST EXAMPLES

The most recent GRC of the Smallville district of Regulated Water Company (RWC) was in 2002, with test years of 2003 and 2004.

Smallville experienced an increase in power costs in March of 2003 and began tracking them in an account. Smallville was granted an offset rate increase in April of 2003. Subsequently, there were additional increases in power cost and additional offsets were approved.

Smallville experienced an increase in purchased water costs in July of 2004 and began tracking them in a separate account. It was granted an offset rate increase in September of 2004.

RWC filed Advice Letter 100 to recover the 2003 power costs in March of 2004.

Advice Letter 100

2003 Purchased Power

Month	Recorded Sales (KCcf)	Recorded Power Consumption (Kwh)	Incremental Expense Rate Change (\$/Kwh)	Incremental Revenue Rate Change (\$/Ccf)	Revenue Component (\$)	Expense Component (\$)	Over or (Under) Collection (\$)	Commercial Paper Rate (%)	Interest (\$)	Accrual (\$)
Jan	240.2	168,600	-	-	-	-	-	4.77	-	-
Feb	237.3	165,600	-	-	-	-	-	4.79	-	-
Mar	234.2	162,400	0.015	-	-	2,436	(2,436)	4.81	-	(2,436)
Apr	247.2	178,400	0.015	0.0111	2,744	2,676	68	4.79	(10)	(2,378)
May	328.6	231,000	0.015	0.0111	3,647	3,465	182	4.81	(10)	(2,205)
Jun	328.4	235,000	0.025	0.0111	3,645	5,875	(2,230)	4.98	(9)	(4,444)
Jul	349.3	242,200	0.025	0.0111	3,877	6,055	(2,178)	5.11	(19)	(6,640)
Aug	342.8	247,000	0.025	0.0193	6,616	6,175	441	5.25	(29)	(6,228)
Sep	333.2	231,100	0.030	0.0193	6,431	6,933	(502)	5.32	(28)	(6,758)
Oct	298.0	206,600	0.030	0.0193	5,751	6,198	(447)	5.88	(33)	(7,238)
Nov	247.3	180,000	0.030	0.0193	4,773	5,400	(627)	5.81	(35)	(7,900)
Dec	207.6	150,000	0.030	0.0193	4,007	4,500	(493)	5.87	(39)	(8,432)
Total Revenue Component					41,492					
Total Expense Comp						49,713				

Step 3.a&c: RWC determines that Smallville district had over earnings of \$36,000 in 2003.

Step 4.a: There is only the purchased power account, which has an expense component of \$49,713.

Step 4.b: The over earning amount is \$36,000, which is less than the total expense component of \$49,713. \$36,000 is recorded as the adjustment amount.

Step 4.c: In a new and separate account (p. 5), \$36,000/12 is booked to each month of 2003.

Appendix H
RECORDED MEANS TEST EXAMPLES

Month	Adjustment (\$)	Commercial Paper Rate (%)	Interest (\$)	Accrual (\$)
Jan-99	3,000	4.77	-	3,000
Feb-99	3,000	4.79	12	6,012
Mar-99	3,000	4.81	24	9,036
Apr-99	3,000	4.79	36	12,072
May-99	3,000	4.81	48	15,121
Jun-99	3,000	4.98	63	18,183
Jul-99	3,000	5.11	77	21,261
Aug-99	3,000	5.25	93	24,354
Sep-99	3,000	5.32	108	27,462
Oct-99	3,000	5.88	135	30,596
Nov-99	3,000	5.81	148	33,744
Dec-99	3,000	5.87	165	36,909

Step 4.d: Interest is applied to the monthly accruals in the adjustment account.

Step 5.: The new expense component is $\$49,713 - \$36,909 = \$12,804$. Because the revenue component exceeds this amount, the account is over collected. Combine the accruals: $(\$8,432) + \$36,909 = \$28,477$.

Step 5.b: The Advice Letter should request a surcredit be applied to the service charge until the amount in Step 5 is refunded.